

**SECTION 2**  
**CHAPTER 1**  
**GUIDELINES TO EVALUATE**  
**INTERNAL CONTROL OVER FINANCIAL REPORTING**

**BACKGROUND AND AUTHORITY**

Developing a comprehensive assessment plan to evaluate internal control over financial reporting is essential to effective implementation of revised OMB Circular A-123. Management is responsible for establishing and maintaining the operational effectiveness and design of the Department's internal control environment. This requires evaluating, testing, and correcting internal controls independent of auditors, including the OIG.

The revised OMB Circular A-123, *Management's Responsibility for Internal Control*, provides updated internal control standards and new specific requirements for conducting management's assessment of the effectiveness of internal control over financial reporting. (See OMB Circular A-123--Appendix A.).

The Department's framework for the assessment is *Standards for Internal Control in the Federal Government*, issued by the GAO in November 1999 (and outlined in Circular A-123). These standards, referred to as the "Green Book," are based on the *Integrated Framework of Internal Control* issued by the Committee of Sponsoring Organizations (COSO). The COSO framework is the most widely applied model in the United States. COSO defines internal control as a process designed to provide reasonable assurance of achieving objectives in three areas: (1) effective and efficient operations; (2) reliable financial reporting; (3) and compliance with applicable laws and regulations. The COSO framework presents five interrelated components, each spanning the three objectives: control environment, risk assessment, control activities, information and communication, and monitoring controls. COSO uses a matrix to illustrate the direct relationship between objectives, control components. The third dimension of the matrix is those units or activities that relate to internal control.

In conducting an evaluation of internal control over financial reporting, personnel should first plan and scope the evaluation. Effective planning is critical. Then, reviewers should document the significant controls, evaluate design and operating effectiveness of control over financial reporting, and document evaluation results. Management must identify and correct deficiencies and report on internal controls in management's written assertion.